

# **Audit**



# **Report**

OFFICE OF THE INSPECTOR GENERAL

**RECOVERY OF DEPRECIATION  
FOR REAL PROPERTY FACILITIES**

Report No. 95-144

March 13, 1995

**Department of Defense**

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### **Acronyms**

DBOF	Defense Business Operations Fund
DLA	Defense Logistics Agency
MILCON	Military Construction



**INSPECTOR GENERAL**  
**DEPARTMENT OF DEFENSE**  
**400 ARMY NAVY DRIVE**  
**ARLINGTON, VIRGINIA 22202-2884**



March 13, 1995

**MEMORANDUM FOR UNDER SECRETARY OF DEFENSE (COMPTROLLER)**

**SUBJECT: Audit Report on the Recovery of Depreciation for Real Property Facilities**  
**(Report No. 95-144)**

We are providing this report for your review and comments. This audit was performed as part of the Inspector General, DoD, Report No. 94-149, "Property, Plant, and Equipment Accounts on the Financial Statements of the Defense Logistics Agency Business Areas of the Defense Business Operations Fund for FY 1993," June 29, 1994. Based on comments received from the Under Secretary of Defense (Comptroller) to a draft of this report, we revised the final report finding, recommendations, and potential monetary benefits.

DoD Directive 7650.3 requires that audit recommendations be resolved promptly. Therefore, we request that the Under Secretary of Defense (Comptroller) provide comments on this final report by April 14, 1995.

The courtesies extended to the audit staff are appreciated. If you have any questions on this audit, please contact Mr. Charles Hoeger, Audit Program Director, in our Philadelphia Office, at (215) 737-3881 (DSN 444-3881) or Mr. John Issel, Audit Project Manager, in our Columbus Office, at (614) 337-8009. The distribution of this report is listed in Appendix C. The audit team members are listed on the inside back cover.

*David K. Steensma*

David K. Steensma  
Deputy Assistant Inspector General  
for Auditing

## Office of the Inspector General, DoD

Report No. 95-144

(Project No. 3LD-2023.01)

March 13, 1995

### RECOVERY OF DEPRECIATION FOR REAL PROPERTY FACILITIES

#### EXECUTIVE SUMMARY

**Introduction.** The Under Secretary of Defense (Comptroller) (Comptroller, DoD) policy on Defense Business Operations Fund (DBOF) funding required DBOF organizations to recover the cost of depreciation of real property facilities, regardless of the source of funds used to finance the construction of the facilities, such as the Military Construction (MILCON) Appropriations and the DoD Components' funds for minor construction. However, Public Law 103-160, November 30, 1993, stated that the recovery of depreciation from real property facilities not funded through DBOF was inappropriate and that DBOF should exclude this depreciation from cost recovery rates. We reviewed the action that the Comptroller, DoD, took to revise DBOF funding policy and cost recovery rates. This audit was limited to the effect of the funding policy on the Defense Logistics Agency's distribution depot business area, and was conducted in conjunction with audit work for the Inspector General, DoD, Report No. 94-149, "Property, Plant, and Equipment Accounts on the Financial Statements of the Defense Logistics Agency Business Areas of the Defense Business Operations Fund for FY 1993," June 29, 1994. For the distribution depots, \$84 million was included in the FYs 1993 through 1995 cost recovery rate for depreciation of real property.

**Objectives.** Our objective was to determine whether the Comptroller, DoD, policy on DBOF funding was appropriately and promptly revised to exclude from cost recovery rates depreciation for projects funded from MILCON and non-DBOF minor construction funds. We also determined whether cost recovery rates established through the budgetary process were appropriately adjusted to comply with congressional direction and whether inappropriately collected charges were repaid to military customers.

**Audit Result.** The Comptroller, DoD, did not promptly revise DBOF funding policy and included in the cost recovery rates of the Defense Logistics Agency distribution depots depreciation for MILCON and non-DBOF funded minor construction projects. As a result, the Defense Logistics Agency distribution depots overcollected \$84 million from Military Departments from FY 1993 through FY 1995 for the services provided. Subsequently, by complying with congressional direction, the Comptroller, DoD, reimbursed the military organizations for the majority of the funds overcollected.

**Internal Controls.** A review of internal controls was not applicable to the issues discussed in this report because we reviewed a funding policy and only one element of a budgeted cost recovery rate.

**Potential Audit Benefits.** We identified potential monetary benefits of \$4.2 million that was not returned to the Military Departments for inappropriate depreciation costs that the distribution depots' business area of the Defense Logistics Agency charged to customers (see Appendix A).

**Summary of Recommendations.** The recommendations presented in the draft report were revised to exclude any reference for the Comptroller, DoD, to reimburse military organizations for the inappropriate recovery of MILCON depreciation costs in the FY 1994 and FY 1995 unit cost rates. We recommend that the Comptroller, DoD, adjust future year cost recovery rates of the Defense Logistics Agency distribution depots to eliminate the recovery of depreciation from non-DBOF funded minor construction projects and initiate action to return any overcollections during FY 1995. We also recommend that the Comptroller, DoD, review all DBOF business area cost recovery rates for FY 1995 to determine whether the rates inappropriately include depreciation costs for non-DBOF funded minor construction projects and if so, initiate action to return any overcollections through reprogramming or other statutory authority provided by Congress.

**Management Comments.** The Comptroller, DoD, did not agree with the audit conclusions in the draft report. The Comptroller, DoD, stated that the facts presented in the background section of the draft audit report did not correctly present the timing involved in the development of guidance for recovery of depreciation from non-DBOF funded real property facilities from FY 1993 through FY 1995. The Comptroller, DoD, also stated that the \$21 million budgeted in FY 1995 for MILCON depreciation was subsequently eliminated. Therefore, the FY 1995 distribution depot rates contained no amount for the recovery of depreciation for MILCON facilities. Furthermore, the Comptroller, DoD, stated that the draft report recommendation to refund FY 1994 and FY 1995 funds related to depreciation does not address congressional action taken involving the cash accounts. The complete text of management's comments is in Part IV.

**Audit Response.** We accept the Comptroller, DoD, actions to reimburse the military organizations for funds overcollected for FY 1993 and FY 1994 due to the recovery of the depreciation from non-DBOF funded real property facilities. We revised the report finding addressing congressional direction to use excess cash generated during FY 1994 to eliminate or reduce advance DBOF billings. For the FY 1994 rates, we agree that using excess DBOF cash to eliminate or reduce advance billings resulted in the military organizations being, in essence, reimbursed for the inappropriate depreciation included in FY 1994 cost recovery rates. For the FY 1995 rates, we agree that the Comptroller, DoD, took proper action in eliminating from cost recovery rates all depreciation costs for the recovery of MILCON funded projects. The recommendations were revised to exclude reference to MILCON depreciation and only address the inappropriate inclusion of non-DBOF funded minor construction depreciation in rates.

The Comptroller, DoD, did not comment on the inappropriate inclusion of non-DBOF funded minor construction depreciation in cost recovery rates. We request that the Comptroller, DoD, provide comments on the final report, revised recommendations, and potential monetary benefits by April 14, 1995.

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This report was prepared by the Logistics Support Directorate, Office of the Assistant Inspector General for Auditing, Department of Defense.

## **Part I - Introduction**

## Background

The Defense Business Operations Fund (DBOF) is a revolving fund that Congress authorized, effective October 1, 1991, by combining existing stock and industrial funds of Defense and Military Department-owned support organizations, such as depot maintenance, distribution depots, and supply management organizations. The DBOF was established to fully identify and ultimately reduce support activities' operating costs through increased efficiencies.

The Under Secretary of Defense (Comptroller) is responsible for developing financial policy for the DBOF organizations. The Comptroller, DoD, "Defense Business Operations Fund Policy," September 27, 1991, required DBOF organizations to recover all operating costs by charging a fee to its various customers, primarily military organizations, for providing requested goods or services. In the costs to be passed on to DBOF customers through fees or cost recovery rates, the Comptroller, DoD, funding policy required that the business areas include the cost of depreciation of real property facilities regardless of the source of funds used to construct the facilities, such as the Military Construction (MILCON) Appropriations' funds and Military Departments' funds for minor construction. MILCON facilities are construction projects that cost more than \$300,000 and receive funding through the MILCON Appropriations. Minor construction is construction of new facilities and repair of existing facilities to change their function or extend their useful life, at a cost of up to \$300,000. Funding for minor construction projects is usually obtained from the Operation and Maintenance Appropriations of the Military Departments or other Defense organizations.

The House of Representatives, Committee on Armed Services Report No. 102-527, "National Defense Authorization Act for FY 1993," May 19, 1992, specified that DBOF should not be charging its customers for recovery of the depreciation of real property facilities that MILCON funded. Subsequently, Public Law 103-160, Defense Authorization Act for FY 1994, Title III, 107 Stat. 1621, November 30, 1993, stated:

Charges for goods and services provided through the Defense Business Operations Fund . . . shall not include amounts necessary to recover the costs of a military construction project (as such term is defined in section 2801(b) of Title 10, United States Code), other than a minor construction project financed by the Defense Business Operations Fund pursuant to section 2805(c) (1) of such title.

The congressional intent was to prevent the recovery of MILCON and non-DBOF funded minor construction projects because such recovery would lead to excess cash in the DBOF. The recovery would also result in such types of real property facilities (that is, facilities that DBOF did not pay for) being paid for twice, once through the appropriations used to finance the construction of the facility and once through higher prices charged to DBOF customers.



The Defense Logistics Agency's (DLA) distribution depots was one of the support activities consolidated in the DBOF. With the implementation of the Defense Management Review Decision 902, all DoD distribution depots were consolidated under DLA. The consolidation gave DLA the authority to manage, use, and maintain hundreds of millions of dollars of real property facilities that had been constructed with MILCON funds for major construction projects and Military Department and DLA funds for minor construction. The primary mission of the DLA distribution depots is to receive, store, and issue supplies to support DoD Armed Forces worldwide.

## Objectives

The objective of the audit was to determine whether the Comptroller, DoD, policy on DBOF funding was appropriately and promptly revised to exclude from cost recovery rates the cost of depreciation from MILCON and minor construction funded projects that DBOF did not pay for. We also determined whether cost recovery rates established through the budgetary process were appropriately and promptly adjusted to comply with congressional direction, and whether inappropriately collected charges were repaid to military customers.

## Scope and Methodology

We reviewed Comptroller, DoD, policy on DBOF funding issued from September 1991 through September 1994. We also reviewed reports from the House and Senate Armed Services Committees on the establishment of DBOF cost recovery rates for FYs 1993 through 1995, as well as applicable public laws.

We examined the DBOF program budget decision documents used to establish the cost recovery rates for DLA distribution depots for FY 1993 through FY 1995. We analyzed distribution depot workload data to determine the actual costs that the depots recovered for the depreciation of non-DBOF funded real property facilities. Even though the Comptroller, DoD, funding policy on depreciation of real property facilities was applicable to all DBOF business areas, our audit was limited to the effect of the funding policy on DLA distribution depots. The audit was conducted in conjunction with audit work on Inspector General, DoD, Report No. 94-149, "Property, Plant, and Equipment Accounts on the Financial Statements of the Defense Logistics Agency Business Areas of the Defense Business Operations Fund for FY 1993," June 29, 1994. The following table displays the budgeted amounts included in the distribution depots' cost recovery rates for the depreciation of non-DBOF funded real property facilities.

## Introduction

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### Budgeted Cost Recovery for Distribution Depots' Real Property Depreciation <sup>1</sup>

	FY 1993 <u>(million)</u>	FY 1994 <u>(million)</u>	FY 1995 <u>(million)</u>
Major construction (MILCON)	\$21.0	\$50.0	\$21.0
Minor construction			
DBOF Funded	0.3	0.7	2.2
Non-DBOF Funded	<u>4.6</u>	<u>4.2</u>	<u>4.2</u>
Total	<u>\$25.9</u>	<u>\$54.9</u>	<u>\$27.4</u>

<sup>1</sup> Prior to passage of the National Defense Authorization Act of FY 1994, November 30, 1993.

To determine the appropriate amount of depreciation costs for minor construction projects that were constructed with DBOF funds and could be included in the cost recovery rates, we used the DLA Real Property Maintenance Database to differentiate between the minor construction projects constructed before the creation of DBOF in FY 1991 and those projects constructed after the creation of DBOF.

We discussed the appropriateness of including depreciation of non-DBOF funded facilities in cost recovery rates with senior management personnel from the Comptroller, DoD, and the Office of the DLA Comptroller. Additionally, we reviewed the future year cost recovery rates for the distribution depots to determine whether appropriate adjustments were made to compensate the Military Departments for inappropriate charges for depreciation previously collected.

This financial related audit was conducted from May through August 1994, in accordance with auditing standards issued by the Comptroller General of the United States as implemented by the Inspector General, DoD. We relied on computer-processed data from the DLA real property maintenance data base to conduct this audit; but because of the nature of the audit, we did not include a complete assessment of the reliability of the computer-processed data. Organizations visited or contacted during the audit are in Appendix B.

## Internal Controls

A review of internal controls was not applicable to the issues addressed in this report because the audit entailed an evaluation of a DBOF funding policy; and we only reviewed the budgetary development of one cost element (that is, depreciation costs for real property facilities of the DLA distribution depots' cost recovery rate).

## Related Audits and Other Reviews

Within the last 3 years, the General Accounting Office provided testimony on two occasions before the House of Representatives, Subcommittee on Readiness, Committee on Armed Services, regarding DBOF established policy for depreciation of MILCON facilities.

General Accounting Office Testimony, T-AFMD-93-4, (OSD Case No. 9339-A), "Financial Management, Opportunities to Strengthen Management of the Defense Business Operations Fund," May 13, 1993, stated that DoD pricing guidance required DBOF business areas to charge its customers the depreciation expense for MILCON facilities even though Congress had directed that those facilities be funded through the MILCON appropriations. Because Congress continued to consider that expenditure a non-DBOF expenditure, the General Accounting Office concluded that including MILCON depreciation in DBOF rates was inappropriate.

General Accounting Office Testimony, T-AFMD-92-8, (OSD Case No. 9057), "Financial Management, Defense Business Operations Fund Implementation Status," April 30, 1992, stated that in developing FY 1993 cost recovery rates, DoD inappropriately included the depreciation of MILCON facilities as part of the total DBOF operating costs. DoD inappropriately included about \$305 million for MILCON depreciation in prices charged to customers. The charges were inappropriate because DBOF does not fund MILCON costs. As a result, MILCON projects were being paid for twice, once through the appropriation and once through higher prices charged to DBOF customers.

## **Part II - Finding and Recommendations**

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## **Recovery of Real Property Depreciation**

Depreciation costs of real property facilities funded by MILCON and minor construction projects not funded through DBOF were inappropriately included in cost recovery rates of the Defense Logistics Agency distribution depots. The condition occurred because the Comptroller, DoD, did not appropriately or promptly revise DBOF funding policy and cost recovery rates to eliminate depreciation costs of non-DBOF funded real property facilities. As a result, Defense Logistics Agency distribution depots overcollected funds from military organizations for goods and services it provided from FY 1993 through FY 1995.

### **Background**

Operating costs are recovered through cost recovery rates that are developed for each DBOF organization based on the estimated outputs (that is, the quantity of goods or services) to be provided by the particular DBOF organization to its customers, generally military organizations. The Comptroller, DoD, establishes cost recovery rates for each DBOF organization through the annual budgetary process. To illustrate, the Comptroller, DoD, established the cost recovery rate for the DLA distribution depots based on DLA budget input of the estimated number of materiel issues and receipts and the estimated annual operating costs. For each issue and receipt of materiel by the distribution depots, costs are recovered through the applicable supply management organization's materiel surcharge. As such, military organizations pay distribution depot costs whenever materiel is ordered through the DBOF supply management organizations.

### **Non-DBOF Funded Real Property Depreciation**

Depreciation costs for non-DBOF funded real property were inappropriately included in cost recovery rates. Before the November 30, 1993, passage of the National Defense Authorization Act of FY 1994, the Comptroller, DoD, funding policy required DBOF organizations to recover all operating costs, including the depreciation of real property facilities whether funded by MILCON or non-DBOF funded minor construction projects. To illustrate, even though DLA did not have records on the actual amount of depreciation costs for real property facilities funded by MILCON, the Comptroller, DoD, estimated that \$21 million in depreciation costs for MILCON funded facilities would be included in the operating costs of the distribution depot for FY 1993, \$50 million for FY 1994, and \$21 million for FY 1995.

## **DBOF Funding Policy and Cost Recovery Rates**

The Comptroller, DoD, did not appropriately or promptly revise DBOF funding policy and cost recovery rates to eliminate the depreciation of non-DBOF funded real property facilities. As a result, the DLA distribution depots overcollected from military organizations \$84 million for goods and services during FYs 1993 through 1995. Further, the Comptroller, DoD, had not compensated military organizations for \$4.2 million in improper charges included in the cost recovery rates in FY 1995. Details on the depreciation costs that were passed on to military customers each year are in the following paragraphs.

**Recovery of Real Property Depreciation in FY 1993.** The Comptroller, DoD, budgeted and included in the cost recovery rates for DLA distribution depots for FY 1993 an estimated \$25.6 million for recovery of the depreciation of real property facilities not funded by DBOF. Of the \$25.6 million, \$21 million was for the recovery of the depreciation of MILCON facilities, and \$4.6 million was for the depreciation of minor construction that DBOF did not pay.

According to Comptroller, DoD, personnel, although the \$25.6 million was charged to and collected from DBOF military customers in FY 1993, the overcollection was reimbursed to the Military Departments as part of the congressionally directed \$5.5 billion transfer of DBOF cash to the Military Departments' operations and maintenance accounts. Public Law 102-396, "Department of Defense Appropriations Act of 1993," required the transfer of DBOF cash, in part, to compensate the Military Departments for improper DBOF fees, such as the \$305 million for the depreciation of MILCON facilities included in DBOF FY 1993 cost recovery rates (see Related Audits and Other Reviews).

**DBOF Cost Recovery Rates for FY 1994.** After the passage of Public Law 103-160, November 30, 1993, which directed that MILCON and non-DBOF funded minor construction not be included in cost recovery rates, FY 1994 cost recovery rates were not adjusted. The distribution depot rates included an estimated \$54.2 million of inappropriate depreciation costs for non-DBOF funded real property facilities. The \$54.2 million consisted of \$50 million of depreciation costs for MILCON and \$4.2 million of depreciation costs for minor construction that DBOF did not finance.

As with FY 1993 collections, the Comptroller, DoD, stated that the military organizations were reimbursed for the overcollections of depreciation costs because Congress specified that no transfers of excess cash should be made during FY 1994. Instead, the excess DBOF cash would be used to address shortfalls in training and readiness programs and unfunded locality pay raises and to eliminate or reduce advance DBOF billings.

**Adjustments to Cost Recovery Rates in FY 1995.** The Comptroller, DoD, took appropriate action to eliminate the \$21 million initially included in the FY 1995 budgeted cost recovery rates for the depreciation of MILCON

## Recovery of Real Property Depreciation

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facilities. However, the FY 1995 rates also included \$4.2 million for the recovery of depreciation for non-DBOF funded minor construction facilities. Corrective action has not been initiated to eliminate the \$4.2 million that should not be included in the cost recovery rates.

## Summary

The DLA distribution depots overcollected funds from military organizations of the DBOF supply management business area for the support provided to them, because the Comptroller, DoD, did not act promptly to revise DBOF funding policy and cost recovery rates to exclude depreciation costs for non-DBOF funded real property facilities. As a result, military organizations were charged \$84 million in inappropriate depreciation costs for FYs 1993 through FY 1995. Because of Congressional direction on the use of excess DBOF cash, the military organizations were reimbursed for overcollections for FY 1993 and FY 1994. Also, the Comptroller, DoD, took proper action to eliminate MILCON depreciation costs included in FY 1995 rates. However, appropriate actions were not initiated to ensure depreciation costs for non-DBOF funded minor construction facilities were eliminated in FY 1995 and future year cost recovery rates. Because our audit addressed only the DLA distribution depots, we did not quantify the inappropriate depreciation costs that were included in surcharge rates of other DBOF organizations. By quantifying the inappropriate depreciation charges, the Comptroller, DoD, can reprogram available funds or, through other statutory authority, reimburse the military organizations for improper charges.

## Recommendations, Management Comments, and Audit Response

**Revised Recommendations.** As a result of management comments, we revised the recommendations to address only the inappropriate inclusion of minor construction depreciation in cost recovery rates.

**We recommend that the Under Secretary of Defense (Comptroller):**

1. Adjust the future year cost recovery rates for the Defense Logistics Agency distribution depots to eliminate the recovery of depreciation for non-Defense Business Operations Fund funded minor construction projects.
2. Initiate action to return the overcollections in FY 1995 by the distribution depots for the recovery of depreciation of non-Defense Business Operations Fund funded minor construction projects through reprogramming or other statutory authority provided by Congress.

**3. Review all remaining Defense Business Operations Fund organizations' cost recovery rates for FY 1995 to determine whether the rates inappropriately include depreciation costs for non-Defense Business Operation Fund funded minor construction projects; and if so, initiate action to return any overcollections through reprogramming or other statutory authority provided by Congress.**

**Management Comments.** The Comptroller, DoD, did not agree with the audit conclusions in the draft report. The Comptroller, DoD, stated that the facts presented in the background section of the draft audit report did not correctly present the timing involved in the development of guidance for recovery of depreciation from non-DBOF funded real property facilities from FY 1993 through FY 1995. The Comptroller, DoD, also stated that the \$21 million budgeted in FY 1995 for MILCON depreciation was subsequently eliminated. Therefore, the FY 1995 distribution depot rates contained no amount for the recovery of depreciation for MILCON facilities. Further, the Comptroller, DoD, stated that the draft report recommendation to refund FY 1994 and FY 1995 funds related to depreciation did not address congressional action taken involving the cash accounts. That is, Congress directed that excess cash be used to eliminate or reduce advance DBOF billings. The complete text of management's comments is in Part IV.

**Audit Response.** The facts as presented in the report correctly present the timing involved in the development of guidance for the recovery of depreciation of real property facilities. However, in response to the management comments, we revised the section of the report finding addressing congressional direction to use excess cash generated during FY 1994 to eliminate or reduce advance DBOF billings. Specifically, we agree that using excess DBOF cash to eliminate or reduce advance billings resulted in the military organizations being, in essence, reimbursed for the inappropriate depreciation included in FY 1994 cost recovery rates.

We also revised the report to show that the Comptroller, DoD, took appropriate action to eliminate the \$21 million budgeted for MILCON depreciation from the DLA distribution depots' rates for FY 1995.

Further, we revised the recommendations and potential monetary benefits to eliminate reference to the inclusion of MILCON depreciation in the cost recovery rates. The revised report discussion and recommendations continue to address the inappropriate inclusion of depreciation costs for non-DBOF funded minor construction facilities in FY 1995 and future year rates. Comments from the Comptroller, DoD, to a draft of this report did not address the inclusion of depreciation of non-DBOF funded minor construction facilities in cost recovery rates.

We request that the Comptroller, DoD, provide comments to the revised finding, recommendations, and potential monetary benefits by April 14, 1995.



## **Part III - Additional Information**

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## Appendix A. Summary of Potential Benefits Resulting From Audit

Recommendation Reference	Description of Benefit	Amount and/or Type of Benefit
1.	Compliance with requirements of "Defense Authorization Act," (Public Law 103-160) by excluding in cost recovery rates the depreciation of non-DBOF funded minor construction projects.	Nonmonetary
2. and 3.	Economy and Efficiency. Provides use of funds from overcollections of depreciation costs included in DBOF cost recovery rates.	Funds put to better use. We estimated that about \$4.2 million could be used for other purposes through reprogramming or other statutory authorized transfers.*

\* The actual amounts available for other uses can be determined only after the Comptroller, DoD, reviews the other DBOF business areas to determine the full amount of non-DBOF funded minor construction depreciation included in cost recovery rates during FY 1995. The Comptroller, DoD, must determine whether DBOF funds are available for reprogramming or other statutory authorized transfers.

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## **Appendix B. Organizations Visited or Contacted**

### **Office of the Secretary of Defense**

Under Secretary of Defense (Comptroller), Management Systems, Washington, DC

### **Defense Organizations**

Headquarters, Defense Finance and Accounting Service, Washington, DC

Defense Finance and Accounting Service, Columbus, OH

Headquarters, Defense Logistics Agency, Alexandria, VA

Defense Distribution Region East, New Cumberland, PA

Defense Depot Memphis, Memphis, TN

Defense Distribution Region West, Stockton, CA

Defense Depot Ogden, Ogden, UT

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## **Appendix C. Report Distribution**

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### **Department of the Navy**

Assistant Secretary of the Navy (Financial Management)  
Auditor General, Department of the Navy

### **Department of the Air Force**

Assistant Secretary of the Air Force (Financial Management and Comptroller)  
Auditor General, Department of the Air Force

### **Defense Organizations**

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Director, National Security Agency  
Inspector General, Central Imagery Office  
Inspector General, Defense Intelligence Agency  
Inspector General, National Security Agency  
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National Security and International Affairs Division, Defense and National  
Aeronautics and Space Administration Management Issues  
National Security and International Affairs Division, Military Operations and  
Capabilities Issues

## **Non-Defense Federal Organizations (cont'd)**

Chairman and Ranking Minority Member of Each of the Following Congressional Committees and Subcommittees:

- Senate Committee on Appropriations
- Senate Subcommittee on Defense, Committee on Appropriations
- Senate Committee on Armed Services
- Senate Committee on Governmental Affairs
- House Committee on Appropriations
- House Subcommittee on National Security, Committee on Appropriations
- House Committee on Government Reform and Oversight
- House Subcommittee on National Security, International Affairs, and Criminal Justice, Committee on Government Reform and Oversight
- House Committee on National Security

## **Part IV - Management Comments**

# Under Secretary of Defense (Comptroller) Comments



COMPTROLLER  
(Program/Budget)

OFFICE OF THE UNDER SECRETARY OF DEFENSE  
1100 DEFENSE PENTAGON  
WASHINGTON, DC 20301-1100



JAN 20 1995

MEMORANDUM FOR DIRECTOR, LOGISTICS SUPPORT DIRECTORATE, OFFICE  
OF THE DOD INSPECTOR GENERAL

SUBJECT: Audit Report on the Recovery of Depreciation for Real  
Property Facilities (Project No. 3LD-2023.01)

The attached provides comments regarding the subject draft  
audit. This office continues to believe, as previously  
discussed with your auditor, that the facts as presented in the  
audit are simply wrong.

This response is forwarded after your due date of January 6  
because no formal copy was received for comment until  
January 17.

Attachment  
As stated

BRUCE A. DAUER  
ASSISTANT DEPUTY COMPTROLLER  
(PROGRAM/BUDGET)

DoD Comptroller Comments on Draft Audit 3LD-2023.01, Recovery of Depreciation for Real Property Facilities

1. The facts presented in the Background of the draft audit report do not correctly present the timing involved and lead to an erroneous conclusion.

The House Armed Services Committee Report for FY 1993 from May 1992 represents report language from one committee. The Senate Armed Services Committee Report and the FY 1993 National Defense Authorization Act did not repeat this House position.

The House Armed Services Committee Report for FY 1994 provided similar report language. The FY 1994 National Defense Authorization Act, dated November 30, 1993, required that charges for Defense Business Operations Fund goods and services not include amounts to recover military construction depreciation, other than minor construction financed by DBOF.

When the 1994 Authorization Act was signed, FY 1994 was two months old. FY 1994 prices had been set 11 months before and were stabilized as a matter of policy. Under stabilized pricing, prices are not adjustable during the fiscal year of execution. In addition, the Congress had indicated that any cash generated in the DBOF was to be used to decrease advance billing.

2. The audit result in the Executive Summary statement that the Comptroller, DoD did not promptly revise DBOF funding policy and included MilCon depreciation in DLA distribution rates is not correct. It does not address fiscal year timing questions explained at length to the auditor.

Following passage of the FY 1994 Authorization Act, FY 1995 DBOF prices, the first prices that could be adjusted, were promptly changed to eliminate all amounts to recover military construction depreciation financed by DBOF.

3. The table on page 4 of the draft audit incorrectly portrays the amount of military construction depreciation budgeted in FY 1995. The table is correct if it intends to depict the FY 1995 value as it existed in the FY 1994 budget. It is incorrect in its portrayal of the FY 1995 value as existing in the FY 1995 budget presented to Congress and as executed. For both of these latter budgets, FY 1995 military construction depreciation is zero.



4. The discussion on page 8 and 9 of the inclusion of \$50 million in military construction depreciation costs for the year FY 1995 is incorrect as stated because it ignores the fact that, except for the FY 1995 column of the FY 1994 budget, budgeted and executed military construction depreciation was zero for FY 1995. This timing aspect is ignored in this presentation.

5. The audit concludes on page 9 that FY 1993 DBOF rates inappropriately included military construction depreciation. The FY 1994 National Defense Authorization Act, which ended this budgeting practice, was signed after the conclusion of FY 1993.

6. The audit finds on page 10 that the adjustment to FY 1995 rates removing military construction depreciation adjusted the wrong amount. The audit confuses the difference between two differing estimates of depreciation, made in different budgets, and is wrong.

Revolving fund rates in DBOF are constructed for each budget based on cost estimates that change. The original estimate for FY 1995 military construction of \$50 million was revised the following year by DLA in its budget estimate to \$21 million. During review of that budget, a Program Budget Decision removed the total military construction depreciation amount (\$21 million).

Costs are budgeted in DBOF rates and DBOF customer accounts are adjusted to meet the rates. DLA Distribution Depot rates for FY 1995 presented to Congress and executed included no military construction depreciation. The difference between the original FY 1995 estimate and the final zero amount was included in the adjustment of all DBOF costs that was applied to the customer accounts.

7. The recommendation that amounts be refunded for FY 1994 and FY 1995 operating results related solely to inaccurately depicted military construction depreciation amounts does not address congressional action taken involving DBOF cash accounts resulting from pricing. Congress has already addressed this issue and the cash impact. Congressional direction was reflected in execution *and the Department is using any DBOF profits to reduce/eliminate advance billing as directed by Congress.*

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